DOCUMENT RESUME

ED 462 099 JC 020 166

TITLE	Los Angeles Community College District: Proposed Reforms Have Not Fully Addressed Past Problems and Create a New Set of Challenges.
INSTITUTION	California State Office of the Auditor General, Sacramento.
PUB DATE	1998-12-00
NOTE	64p.
AVAILABLE FROM	California State Auditor, Bureau of State Audits, 555 Capitol Mall, Suite 300, Sacramento, CA 95814 ($3). Tel: 916-445-0255; Web site: http://www.bsa.ca.gov/bsa/.
PUB TYPE	Reports - Descriptive (141)
EDRS PRICE	MF01/PC03 Plus Postage.
DESCRIPTORS	Budgeting; *Community Colleges; Educational Economics; *Educational Planning; Finance Reform; *Financial Audits; Financial Policy; *Financial Problems; Institutional Administration; Money Management; Two Year Colleges
IDENTIFIERS	California (Los Angeles); Los Angeles Community College District CA

ABSTRACT

This report was conducted by the California State Auditor to examine the fiscal problems facing the Los Angeles Community College District. It is divided into four chapters. Chapter 1, "Costly Policies and Poor Management Have Led to the District's Deteriorating Fiscal Condition," describes the financial downturn the district has experienced since 1995. Findings implicate ineffective budgeting practices, lack of accountability, and poor management and planning as reasons for the problems. Chapter 2, "Limited State and Local Funding Contributes to the Deteriorated Physical Condition of Facilities in the Los Angeles Community College District," addresses the fact that external funding has not kept up with the needs of the institutions. The auditors suggest that the district be more proactive in its capital outlay planning and align its maintenance project priorities with those of the states to ensure funding. Chapter 3, "Current Reforms Have Yet To Resolve the District's Fiscal Problems and Will Create New Challenges," highlights the recent reform movement toward decentralizing administration. Although such reform was implemented to combat previous fiscal challenges, it has been ineffective thus far and has introduced additional concerns to the system. Chapter 4, "Conclusion and Recommendations," offers several suggestions for approaching and improving the financial situation. The district's response to the audit and the auditor's ensuing comments are appended. (JCC)

California State Auditor

BUREAU OF STATE AUDITS

Los Angeles Community College District:

Proposed Reforms Have Not Fully Addressed Past Problems and Create a New Set of Challenges

December 1998
97107

The first copy of each California State Auditor report is free. Additional copies are $3 each. You can obtain reports by contacting the Bureau of State Audits at the following address:

California State Auditor
Bureau of State Audits
555 Capitol Mall, Suite 300
Sacramento, California 95814
(916) 445-0255 or TDD (916) 445-0255 x 248

OR

This report may also be available
on the worldwide web
http://www.bsa.ca.gov/bsa/

CALIFORNIA STATE AUDITOR

ELAINE M. HOWLE
STATE AUDITOR

STEVEN M. HENDRICKSON
CHIEF DEPUTY STATE AUDITOR

December 23, 1998 97107

The Governor of California
President pro Tempore of the Senate
Speaker of the Assembly
State Capitol
Sacramento, California 95814

Dear Governor and Legislative Leaders:

As requested by the Joint Legislative Audit Committee, the Bureau of State Audits presents its audit report concerning the Los Angeles Community College District, the causes for its recent fiscal difficulties, the manner in which it handles its budgetary problems, and the status of its current reform efforts.

This report concludes that its costly decisions on employee agreements and other matters and poor management practices have contributed significantly to the district's fiscal problems. In particular, its ineffective budgeting and lack of accountability have prevented the district from promptly reacting to fiscal problems and have resulted in overspending and depletion of reserves. The district's reform efforts are in an early stage, but have not yet fully addressed the practices that have contributed to the current fiscal problems. Moreover, the board's decision to decentralize district administration creates a new set of challenges. Furthermore, we believe the run-down condition of some college facilities, caused primarily by lack of state and local funding, is severe enough to discourage some students from enrolling.

Respectfully submitted,

Kurt Sjoberg

KURT R. SJOBERG
State Auditor

BUREAU OF STATE AUDITS
555 Capitol Mall, Suite 300, Sacramento, California 95814 Telephone: (916) 445-0255 Fax: (916) 327-0019

Los Angeles Community College District:

Proposed Reforms Have Not Fully Addressed Past Problems and Create a New Set of Challenges

CONTENTS

SUMMARY

Audit Highlights . . .

The Los Angeles Community College District has been facing financial uncertainty.

Our report revealed:

- ☑ ***Costly board policies and poor management at all levels have significantly contributed to the district's fiscal woes.***
- ☑ ***Despite showing some promise, current reforms have not yet fully addressed past problems.***
- ☑ ***Decentralization efforts create new challenges the district must address.***
- ☑ ***State and local funding has not kept pace with the district's unmet facility needs. As a result, the physical condition of some campus facilities is poor. If facilities deteriorate further, safety concerns may arise and fewer students may enroll in the district's colleges.***

RESULTS IN BRIEF

The Los Angeles Community College District (district), composed of nine colleges and a district office that provide educational services to approximately 100,000 students, is the largest in the State. In December 1997, its independent financial auditors warned that the district might not remain financially viable. Moreover, the Accrediting Commission for Community and Junior Colleges expressed extreme alarm in January 1998 about this opinion and cited specific concerns about district-level planning, budgeting, administrative stability, and fiscal health.

Our review focused on the causes of the district's fiscal and budgetary difficulties and how the district plans to address them. We found that costly policies and poor management have contributed significantly to the district's poor fiscal condition. For example, the board agreed to salary increases for district employees and allowed excessive overtime for campus police officers, which significantly increased costs. In addition, ineffective budgeting practices and lack of accountability have prevented the district from promptly reacting to its fiscal problems and have resulted in overspending and depletion of district reserves. The district's ability to effectively deal with its fiscal problems has been hampered by its lack of cohesive long-range planning, the terms of agreements the board has negotiated with employee unions, and state requirements for the use of full-time faculty. As a result, the district continues to face financial uncertainty.

Many college facilities are run down and in need of repair. While we did not find conditions that raise serious and immediate safety concerns, we believe the poor condition of the facilities is severe enough to affect students' decisions to attend the colleges. The lack of funding at the state and local level hampers needed repairs, improvements, and ongoing maintenance.

Finally, the district is undergoing reforms, a primary feature of which is a decentralization process to vest more decision-making authority with the college presidents. While the district initiated these reforms in response to its fiscal problems, plans to date

have not adequately addressed the costly decisions and poor budgeting practices that historically contributed to these problems. Additionally, the decision to decentralize creates a new set of challenges that the district must address amidst its current fiscal difficulties. For example, the district will need to clarify roles and responsibilities and articulate the new system of internal controls it envisions.

RECOMMENDATIONS

To improve its decision making and guide its reform efforts, the district needs to develop a comprehensive vision for the future that clearly spells out the roles of the board, the district office, and college administrators. This vision should include goals and objectives for the district and the individual colleges that are linked into a consistent, cohesive framework against which all parties can evaluate the merits of proposed management decisions.

To avoid overspending and further eroding its fiscal condition, the district should enforce budgetary and spending controls, including the following:

- Require that colleges base their budgets on realistic estimates of planned activities justified in light of historical expenditures and detailed plans for more efficient use of resources.

- Ensure that appropriate administrators at each college are held accountable for developing and adhering to approved budgets.

- Deny payments if colleges attempt to spend beyond their budgets.

- Ensure that funds are available to cover any increased costs and that terms are consistent with the need to maintain administrative flexibility when negotiating new agreements with its employees.

- Ensure that appropriate action is promptly taken on anticipated budget shortfalls.

To improve the condition of its facilities, the district should consider using savings it achieves in other areas to fund maintenance projects and continue to request funding from the State for needed projects.

The district's efforts to decentralize should include the following:

- Making the presidents' responsibilities commensurate with their authority.
- Ensuring the district can continue to meet its districtwide obligations, statutory or otherwise.
- Determining how it will ensure that the good of the district as a whole prevails in an environment of potentially increased competition among the individual colleges.

Finally, the district should ensure that its decisions on reform result in efficient administration, and cost savings, while preserving basic educational services.

AGENCY COMMENTS

The district agrees with our recommendations and believes it can make improvements in a number of areas our report identifies. It is addressing its fiscal issues and expects to end the current fiscal year with an adequate balance in its unrestricted general fund. ■

INTRODUCTION

The Los Angeles Community College District (district) is the largest in the State, providing educational services for approximately 100,000 students. The district is 1 of 71 districts in the California community college system, and 1 of 20 that currently have multiple campuses. The district is made up of a central district office and 9 colleges. While many of the colleges offer both traditional academic and vocational programs, Trade Technical College specializes in providing vocational classes.

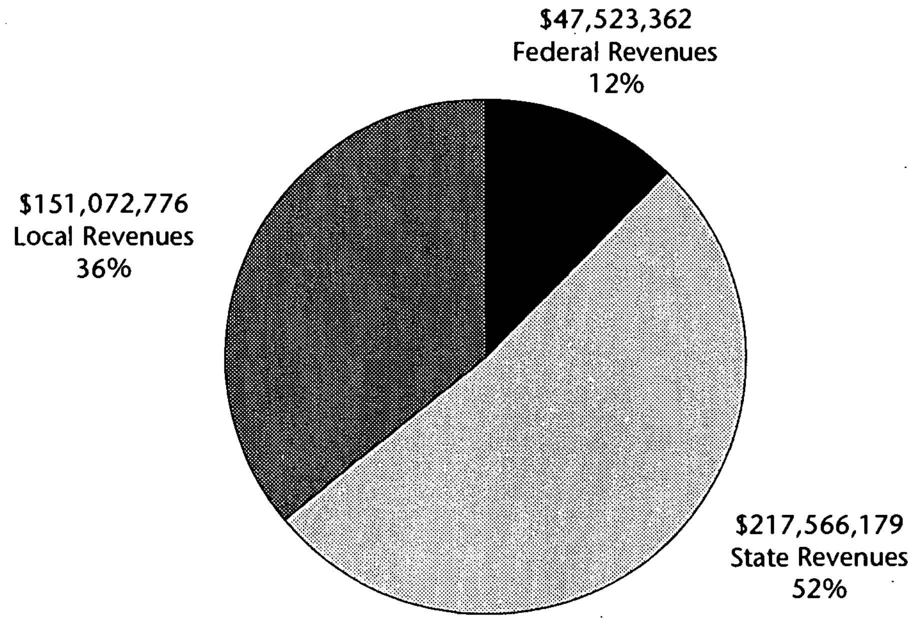
The Chancellor's Office of the California Community Colleges (state chancellor's office) and its board of governors provide leadership to California's community colleges, establishing statewide policies and overseeing some educational and fiscal activities; however, the district is directly governed by a seven-member board of trustees (board) elected by the district's voters to four-year terms. The students annually elect a nonvoting eighth member to the board. The district chancellor implements the board's directives and executes its policies. The role of the district office is to oversee the colleges and establish the day-to-day regulations that govern the district activities. Each of the nine colleges is managed by a president. The faculty, staff, and students have the right to participate in district and college governance, as well. As Figure 1 indicates, for fiscal year 1997-98, the district had approximately $416.2 million in revenues, of which $217.6 million was from the State, and $397.1 million in expenditures.

COLLEGE CAMPUSES, THE DISTRICT OFFICE, AND THE BOARD OF TRUSTEES ALL ARE RESPONSIBLE FOR DEVELOPING THE DISTRICT'S BUDGET

The district's budget development requires a lengthy process that takes nearly a year and involves input from the college presidents and various constituencies, such as the academic senates, faculty, union representatives, and students. Each administrative level—the presidents, the district office, and the board—is responsible for ensuring the budget is reasonable and meets the needs of the district. First, the colleges prepare their

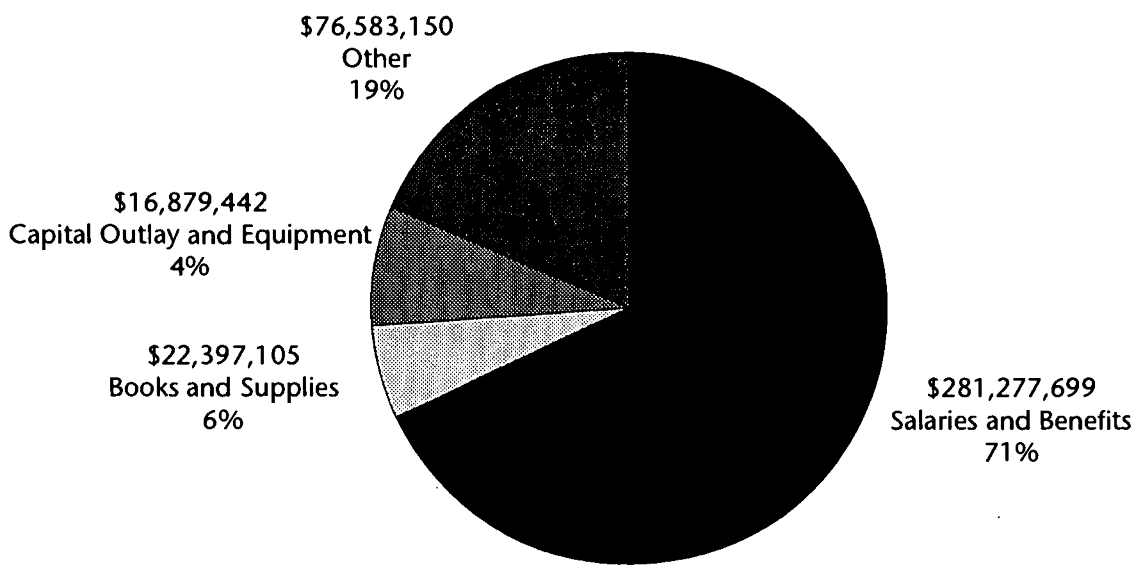
FIGURE 1

Revenue Sources for All Funds
Fiscal Year 1997-98



Source: *Report on Audited Financial Statements for June 30, 1998.*

Expenditure Categories for All Funds
Fiscal Year 1997-98



Source: *Report on Audited Financial Statements for June 30, 1998.*

budget proposals with guidance from their planning advisory committees. The colleges submit the proposals to the district office where staff review them for reasonableness and provide college administrators with analyses of their proposals. The district submits a tentative budget incorporating the colleges' proposals to the board for adoption before July. District office staff incorporate any additional changes into a final budget, which the board must adopt by September 15. However, the district continues to revise the final budget throughout the year as new information about revenues and expenditures becomes available.

THE DISTRICT IS FACING SERIOUS FINANCIAL PROBLEMS

Recent events have raised serious concerns about the district's finances as well as its ability to operate within its budget. In November 1997, the district's independent financial auditors issued an opinion that expressed concerns that the district might not be able "to continue as a going concern." Additionally, in January 1998, the Accrediting Commission for Community and Junior Colleges (commission), which evaluates and accredits institutions with two-year associate degree programs, expressed its "extreme alarm" about the independent auditors' opinion and raised concerns about maintaining accreditation of one or more district colleges. Accreditation certifies to the general public that the district has the resources to accomplish appropriate goals, can demonstrate that it is accomplishing these goals, and gives reason to believe it will continue to do so. The commission's concerns centered on district-level planning, budgeting, administrative stability, and fiscal health. The loss of accreditation, which occurs very infrequently among these institutions, would constitute a serious setback to the district.

As further evidence of its troubled financial state, although the district has been on the state chancellor's office watch list for financially troubled districts during the last nine years, in January 1998, the state chancellor's office downgraded it from Priority 3 to Priority 2 status. This change signals increasing concern that the district's fiscal problems could soon necessitate an emergency apportionment of state money. If the financial condition declines to Priority 1 status, the state chancellor's office may appoint a fiscal monitor. The district's independent financial auditors did not raise concerns about the district's

continued financial viability in the fiscal year 1997-98 opinion, as they did for the prior year, although the district ended the year with a $3 million deficit in its unrestricted general fund.

THE DISTRICT HAS BEGUN REFORMING ITS ADMINISTRATION

Partially to address its financial problems, the district has begun to implement reforms, a primary feature of which is decentralizing its administration. In April 1998, the board voted to decentralize by July 1, 1998 or, if legal impediments existed to certain of the reforms by that date, as soon as legally possible. In supporting decentralization, the board expressed its position that the district's centralized bureaucracy stifled the creativity and flexibility of the colleges, which each serve a unique community. The board anticipated, among other things, that decentralization would enable the district and its colleges to operate more efficiently and would establish a system of accountability to ensure greater financial and educational viability. Since the board's decision, committees representing various interests within the district, including the college presidents, the district chancellor's office, the unions, and the academic senates, have begun studies to determine what functions the district can decentralize.

SCOPE AND METHODOLOGY

The Joint Legislative Audit Committee requested that the Bureau of State Audits conduct an audit of the Los Angeles Community College District's financial position, causes for its recent budget difficulties, the manner in which the district handles budget problems, and its allocation of resources. We were also asked to determine whether the district's policies and procedures ensure that allocated funds are used appropriately and as intended. Additionally, the committee asked that we review and assess the district's capital outlay planning, allocation, and approval process; the condition of the physical facilities; the consistency of auxiliary activities with the district mission and goals; and the use of full- and part-time faculty.

To understand the district's responsibilities and operations, we reviewed the laws, regulations, rules, and policies relevant to the district in general and to the audit request in particular.

As part of our assessment of its financial position, we interviewed district office and college administrators and staff, and analyzed relevant financial and policy documents, to gain an understanding of the district's budgeting process and internal controls and to identify causes of its current financial problems. To assess the extent and effectiveness of district actions to date, we also examined the documents describing the district's decentralization efforts and its other actions to resolve financial problems.

To assess its method of allocating resources among the colleges, we compared the district's current allocation model to that of the state chancellor's office, on which the district's model is partially based, and the conceptual plan the board adopted. We then determined whether the district followed its model in allocating resources to its colleges. To determine whether the district used funds appropriately and as intended, we reviewed district policies and procedures and the independent financial auditor's reports from the past three years.

In reviewing and assessing the district's capital outlays for its physical facilities, we visited each of the nine campuses and the district office, and interviewed appropriate staff at the district, selected colleges, and the state chancellor's office, to gain an understanding of the State's and district's processes for allocating money to capital outlay and scheduled maintenance projects. To determine if the condition of the facilities had a negative impact on student security, safety, and access, we reviewed related documents, such as accident and police reports.

We examined the monitoring and reporting requirements related to the district's auxiliary and enterprise organizations and reviewed annual financial reports. For those organizations with very limited expenditures, we performed no further analysis. For the campus bookstores and cafeterias, we determined whether they were self-sufficient.

In assessing the district's use of full- and part-time faculty, we considered state and district requirements regarding the use of faculty and relevant agreements between the district and the faculty union. We obtained an understanding of the method by which the district calculates its full-time faculty ratio, then compared it to those of other districts across the State. ■

CHAPTER 1

Costly Policies and Poor Management Have Led to the District's Deteriorating Fiscal Condition

CHAPTER SUMMARY

Since fiscal year 1995-96, the district's unrestricted general fund balance available for expenditure in future years has declined significantly and may continue to decline in fiscal year 1998-99. Costly decisions, poor budget practices at all levels, and inadequate controls over spending have led to this deterioration of the district's fiscal condition. The difficulties the district faces in addressing its fiscal problems are exacerbated by its lack of long-range planning and a state requirement related to the use of full-time faculty.

THE DISTRICT'S FINANCIAL RESERVES HAVE DECREASED SIGNIFICANTLY

In early 1998, concerns over the district's deteriorating financial condition reached a critical point when the district projected a $13 million deficit in its unrestricted general fund for the fiscal year ending in June 1998. The unrestricted general fund provides the primary budgetary allocations for the district's operations. To address the projected shortfall, the district enacted measures intended to reduce costs and increase its receipts. On February 25, 1998, the board of trustees (board) ordered the colleges and the district office to terminate all temporary, unrepresented employees; restrict all nonsalary expenditures and funding for facilities projects; and apply for available refunds from the district's insurance carriers. The district realized some additional relief when state and other revenues increased beyond projected amounts.

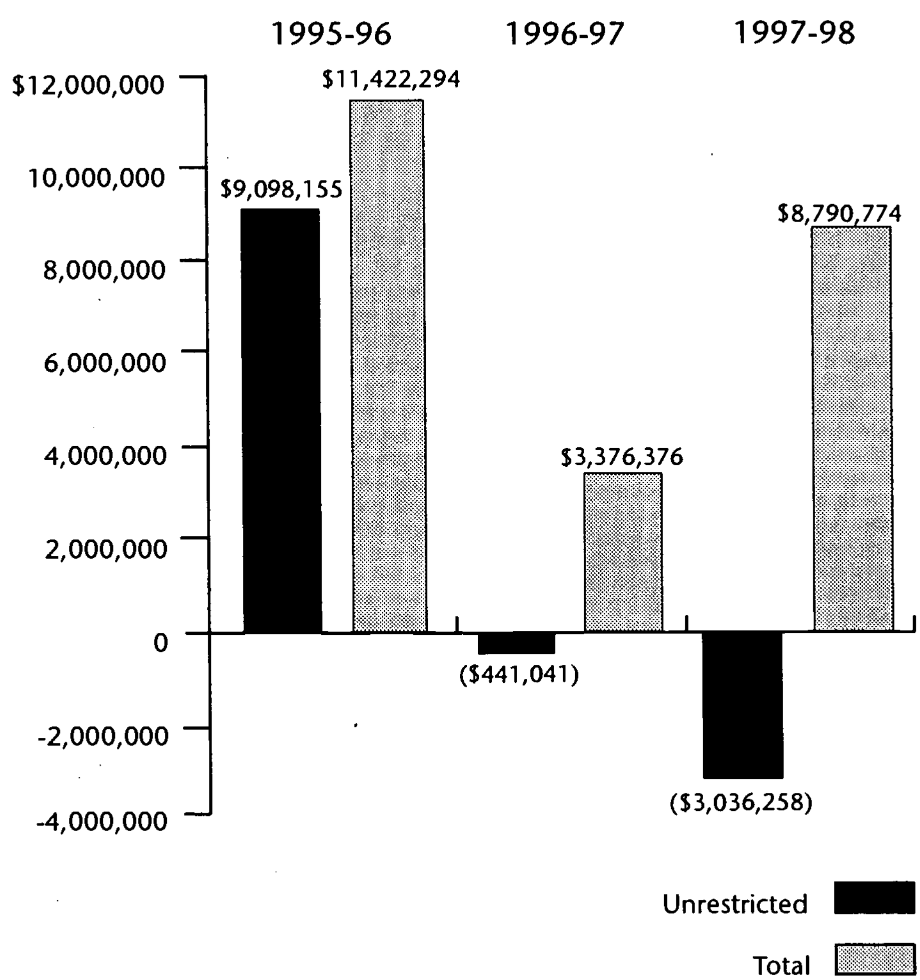
In May, the board voted to transfer approximately $4 million in other funds to cover expenditures originally planned for the unrestricted general fund. The combined effect of the reduced costs, increased revenues, and substitutions of other resources resulted in a smaller operating loss of $3.9 million and a positive

$2.7 million unrestricted general fund balance at the end of the fiscal year. However, after adjustments to comply with generally accepted accounting principles, the district's unrestricted general fund had a deficit balance of $3 million. Although the district was able to mitigate its shortfall, the district office had notified the board of a projected deficit early in fiscal year 1997-98, long before the board took the above actions.

The district's practice of spending more than it receives has caused significant reductions in the unrestricted general fund balance. As Figure 2 indicates, the balance has declined by over $12 million in the last two years.

FIGURE 2

Unrestricted General Fund Balances Have Decreased Since Fiscal Year 1995-96



Source: The Reports on Audited Financial Statements for each fiscal year.

THE DISTRICT HAS MADE COSTLY DECISIONS, CONTRIBUTING TO ITS FINANCIAL DIFFICULTIES

Decisions that have significantly contributed to the district's deteriorating financial condition include making costly agreements with unions representing district employees, purchasing a building to house the district office and subsequently renting another building that currently exceeds the district office's needs, allowing excessive overtime for district police officers, subsidizing the operations of certain campus cafeterias that are not self-supporting, and allowing other provisions in the faculty union agreement that may limit the district's ability to cut costs. Unless it takes action, most of these decisions will continue to affect the district in future years.

The Board Entered Into a Salary Agreement That Significantly Increased Its Costs

The board did not know the full impact of the salary increase at the time it agreed to the contract.

The district has significantly increased salary and benefit costs, partly as a result of an agreement with the faculty union. In February 1997, the president of the district's Board of Trustees (board) and district administrators signed an agreement with the American Federation of Teachers College Guild covering almost three years, from September 30, 1996 through June 30, 1999. When the board agreed to the raises stated in the union contract, it did not base its decision on complete projections of the costs of the salary increases to the district. The district was also unable to demonstrate that it estimated the full impact of the salary increases at the time the board agreed to the union contract.

The precise financial impact of this agreement is difficult to quantify because, for the 1996-97 fiscal year, the agreement established new salary ranges for full-time faculty, but the percentage increases over prior ranges are not specifically stated and are not uniform. Thus, the financial impact depended on the number of faculty at each step of the salary range. Nevertheless, the district estimated the fiscal year 1996-97 increase from the agreement to be 6 percent, in addition to the 2.75 percent cost of living increase already provided in the previous agreement, with increases of 6 percent and 4 percent in the next two years. In addition to these increases, the agreement apportions to the faculty a share of the state revenue derived from the district's growth in attendance for fiscal years 1997-98 and 1998-99, which the district has indicated will be approximately $1.3 million and $.8 million, respectively. During this

period, salaries for other district employees also increased. As Table 1 indicates, the annual unrestricted general fund salary and benefits costs for all staff were $209 million in fiscal year 1995-96, while the district's final budget allots an estimated $243 million in fiscal year 1998-99 for these costs. However, we believe this figure may be low and estimate an amount closer to $251 million. Our estimates closely parallel those the district itself calculated in June 1998, based on the terms of agreements with unions and assuming similar usage of staff. Because we have seen no specific and detailed plans for a different use of staff, we have not attempted to estimate potential efficiencies that could result from changing workload or numbers of staff.

TABLE 1

Staff Compensation Has Increased Significantly

Fiscal Year	Total Salary and Benefits	Increase Over Prior Year Dollars	Increase Over Prior Year Percent
Actual Cost 1995-96[a]	$209,355,882	NA	NA
Actual Cost 1996-97[a]	229,212,096	$19,856,214	9.48%
Actual Cost 1997-98[a]	240,186,874	10,974,778	4.79
District Final Budget 1998-99	242,979,821	2,792,947	1.16
State Auditor Estimate for 1998-99[b]	251,359,418	11,172,544	4.65

[a] Data obtained from the actual expenditures provided in the district's final budgets for fiscal years 1996-97 through 1997-98.

[b] These 1998-99 salary and benefit costs represent our estimates based upon the costs for the previous year and the percent increases authorized in the union agreements.

Table 1 summarizes all unrestricted general fund salary costs and benefits, including increases authorized in union agreements with other employee groups, raises and promotions, and hiring of additional staff. As the table indicates, costs have risen substantially, largely due to union agreements. Using the most recent data, from fiscal year 1996-97, submitted by community colleges and compiled by the State Chancellor's Office of the California Community Colleges (state chancellor's office), we found the average salaries of certificated staff in this district were lower than the averages in most other districts. While we recognize the need for the district to maintain competitive salaries, we nevertheless question how prudent such increases are when the district is experiencing financial problems.

Further, the statewide data suggests that the Los Angeles district had higher than average costs for benefits overall and for salaries for its classified staff. Costs of benefits of 28 percent reported in the Los Angeles district were significantly higher than the state average of 22.8 percent. Total classified salaries were markedly higher in proportion to certificated salaries than the statewide average. In Los Angeles, classified salaries were 62.4 percent of certificated salaries, whereas the average for all community college districts was 52.9 percent. The higher costs suggest that the district had a higher pay scale for classified staff, paid more overtime for classified staff, or had proportionately more classified staff than the average district. In any case, the district's close scrutiny of these costs for benefits and classified staff could provide useful information as the district deals with its financial problems.

Excess Space for District Office Operations Is Costly

The district leases unused office space in one building while continuing to pay debt on another building it has never occupied and may have to sell at a loss. With the potential transfer of district office staff to college campuses under decentralization, the unused space at the district office may increase.

The district will pay millions of dollars for debt on a building it has never occupied.

The district has never occupied a property it purchased at 4050 Wilshire Boulevard. The district purchased the property in 1990 for $12.5 million, earmarking $17.5 million to cover the purchase price, plus $5 million in planned renovations, from a $30 million debt issue. In 1992, the district refinanced the debt by issuing new certificates of participation, documents similar to bonds which represent an undivided interest in payments made under a financing lease. To date, we estimate that the district has paid $18.6 million in debt-service and maintenance costs for this property. The property is currently in escrow with an expected sales price of $5.9 million. The district plans to use the proceeds from the sale to pay off some of the remaining debt, but proceeds will not be sufficient to extinguish all the debt related to this property. Using a revised debt-service schedule provided by the district, we estimate that if it makes payments as currently scheduled, the district will make principal and interest payments of approximately $40.7 million until the year 2018, resulting in total costs related to this building of $59.3 million.

The board has authorized the district to enter into a commitment that would allow the district to refinance the debt on this property in 2002 at a potentially lower rate, if it results in current savings of $1.4 to $2 million. Our investment consultant has described the commitment as a complicated, but not unusual, swap transaction with Salomon Smith Barney followed by a refunding transaction, and indicated that any savings would be the result of reductions in interest rates since the district issued the debt in 1992.[1] According to our consultant, although the commitment would involve some risk, primarily related to ensuring that the district's variable receipts and payments for these transactions remain equal, that risk could be mitigated, as we describe in our recommendations in Chapter 4.

The district's decentralization efforts may cause additional vacancies in its leased office building.

The district decided not to occupy the building at 4050 Wilshire because, based on a brokerage firm's analysis, it was less costly to lease different space for a district office. Instead, it entered into a 12-year lease for another building. According to its vice chancellor of operations, the district planned to utilize the entire building for district office staff. However, until about two years ago, another tenant occupied one of the nine floors. Since the other tenant departed, the space has remained empty and, as of September 1998, we estimate the costs for the space to be $15,000 per month. Further, if the district fully implements its plan to decentralize administration, it may relocate additional office positions to the colleges or eliminate them, resulting in more unused space the district is obligated to pay for unless it can sublet portions of the building. Although the district has been trying to sublet available space, subletting may be difficult, especially at lease rates comparable to what the district is currently paying. A grand jury report on the district's purchase of

[1] The proposed transaction has two parts: 1) a forward fixed-for-floating interest rate swap between Salomon Smith Barney and the district, and 2) a refunding in 2002 of the debt issued in 1992. The district, would be liable to make fixed payments to Salomon Smith Barney under the swap agreement and variable payments on the new debt issued in 2002. In return, Salomon Smith Barney would make variable payments to the district that are intended to equal the variable payments the district would make on the 2002 debt. The intent of the swap is that variable payments the district receives from Salomon Smith Barney under the swap agreement would approximately offset the variable payments on the 2002 debt. The net result intended from the plan is the district's creation of fixed rates for itself for the 2002 refinancing debt that are lower than it is currently paying on the 1992 debt. Its risk is that the variable amounts it receives from Salomon Smith Barney will be less than the variable amounts it pays on the 2002 debt.

the 4050 Wilshire building and the leasing of the current district office building, issued during the 1993-94 fiscal year, indicated that subletting could be difficult because of the building's design. The grand jury concluded that individual floors are not easily subdivided and are therefore less marketable.

The grand jury's primary mandate was to assess whether the district acted improperly or without adequate guidance in the purchase of the 4050 Wilshire building, and in entering into the lease for the current district office building. In each case, the grand jury concluded that the procedures the district followed were common practice for public sector agencies. Although the building lease extends for 12 years, it has an option to renew for an additional 8 years. If the district does not exercise that option, its rent for years 11 and 12 increases dramatically over the current $1.6 million annually, to $5.9 million in year 11 and $6.4 million in year 12. The grand jury concluded that the district would most likely have to occupy the district office building for the entire lease term, including the option period. Thus, both buildings are likely to drain district resources for years to come.

The District Has Paid Excessive Overtime to District Police Officers

Because the district must first offer overtime to full-time police officers under its union agreement, during 1997-98 it incurred $500,000 in excess salary costs.

Excessive overtime costs for campus police officers also contribute to the district's fiscal problems. According to data the district compiled, these costs have exceeded $1 million in each of the last three years. Specifically, the district paid $1.4 million in overtime to campus police in fiscal year 1997-98, over one-third of their regular salary costs of $3.7 million. Moreover, using the data provided, we calculated that the campus police departments could have saved at least $500,000 in fiscal year 1997-98 by using part-time officers rather than paying full-time officers for overtime work. However, the contract the district negotiated with the union required that two police officers work each shift on each campus and that full-time district officers receive priority for overtime work before any part-time help is used. Further, the contract required a permanent freeze on the hiring of all part-time officers. Thus, the district agreed to a union contract that ensured the use of higher-paid employees for overtime work. The contract expired in January 1998 and has not been extended as of November 1998.

Another factor that may contribute to the police overtime costs is understaffed campus police departments. According to information the district provided us, in fiscal year 1997-98, 83 police officers worked more than 45,500 overtime hours, an average of 550 hours per officer. Overtime ranged from 2 to 1,350 hours per officer, with ten officers working over 1,000 hours each. In addition to the effect on labor costs, we question the wisdom of allowing so much overtime, which can impair work performance, for a staff that ensures campus safety.

As of October 1998, the district had 17 vacant police officer positions and no employment eligibility list.

Even without using part-time police officers, the district could reduce overtime costs by hiring more full-time officers and could assign overtime more evenly to all officers. However, the colleges are unable to hire new full-time officers because the district has not completed a police eligibility list. The previous list expired in January 1997. Although the district began the police examination process for the eligibility list in October 1996, several factors have delayed the process, according to the vice chancellor of operations. These include discussions with the police union regarding background checks, decisions about whether police operations should be centralized or decentralized, and the reluctance of college presidents to hire more officers due to fiscal constraints. In September 1998, the board approved a $30,000 contract to use an outside service for background checks. However, as of October 1998, although it had 17 vacant positions, the district had still not completed the police eligibility list. Filling all the vacant positions may not eliminate the need for overtime, but hiring more full-time officers could benefit the district by reducing overtime costs and hours worked by campus officers.

The district's agreement with the police officers' union further ties its hands for overtime assignments. The agreement requires that the union representative on each campus assign overtime based on this rigid system of priorities:

- Permanent full-time officers have priority over permanent part-time officers, captains, lieutenants, or anyone else.

- All permanent full-time officers on a campus who want to work overtime have first priority, in order of seniority.

- All permanent full-time officers on other campuses who want to work overtime on the assigning campus have next priority, again in order of seniority.

- Finally, permanent part-time and retired officers, in order of seniority, can be assigned.

If the district spread out overtime assignments more evenly among all officers, it could likely reduce excessive overtime.

The District Has Subsidized Unprofitable Cafeterias

Another factor contributing to the district's financial problems is its subsidies of unprofitable campus cafeterias, which are accounted for in its cafeteria fund. Historically, the district's cafeteria fund has operated at a loss of thousands of dollars each year. For example, cafeteria operational costs exceeded revenues by $862,000 and $441,000 in fiscal years 1996-97 and 1997-98, respectively. As a result, the district used $1.3 million in general fund money to subsidize campus cafeterias for these two years alone, even though the cafeterias are intended to be self-supporting. Over the past six years, the district used a total of $3.4 million of general fund moneys, through interfund transfers, to subsidize the cafeteria operations.

In 1992, in an effort to improve cafeteria operations, the district adopted a five-year master plan to increase revenues, reduce costs, and eliminate the cafeterias' dependency on general fund support. Because the cafeteria fund continued to need subsidies, the district later retained a consultant to develop a strategic food service plan for each of the colleges' cafeterias. According to the consultant's July 1996 report, the facilities did not meet the consumers' minimum expectations for menu diversity, food quality, or sanitation. It further stated that most of the facilities were deteriorating and outdated. These conditions clearly contribute to the cafeterias' poor performance.

A consultant estimated that the district could generate $625,000 annually by introducing fast food restaurants on campuses, but would require $2.1 million in capital improvements.

The consultant's strategic food service plan contained suggestions for improving customer service and profitability, such as recommendations to develop a facilities master plan to renovate and maximize current space, focus on customer needs instead of production capabilities, and introduce fast-food restaurant chains. The consultant estimated that the district could generate $625,000 annually in profits if it implemented the recommendations. However, the cafeterias would need approximately $2.1 million in capital improvements to make the recommended renovations. In addition, the consultant noted that the requirement to use its own employees to operate any fast-food restaurants on campus represented another barrier for the district to successfully implement the plan.

District and college administrators do not consider renovating the cafeterias to be as high a priority as other scheduled maintenance needs. Although the district has received proposals for campus convenience stores from contractors willing to finance capital improvements if the district reimbursed them from future revenues, the district has allowed the individual campuses to make the decisions about their cafeteria operations. According to the board president, the board approved a pilot program for a commercial food service chain at one of the campuses. However, three colleges currently have no food service operations and the general fund continues to subsidize cafeterias at the remaining campuses.

Certain Provisions of Union Agreements May Unnecessarily Limit the District's Ability to Create Efficiencies

In addition to the salary increases discussed earlier, the district agreed to other provisions in its faculty union agreements that may limit its ability to efficiently operate the district and solve its current problems. In the table below, we compared the agreements of the four largest community college districts in California, including Los Angeles.

TABLE 2

Comparison of Terms in Faculty Union Agreements Signed by the Four Largest Community College Districts

Attributes	Los Angeles	Los Rios	San Diego	San Francisco
Number of campuses	9	3	3	1
Resident full-time equivalent students in 1997-98	71,162	36,104	39,986	33,669
Full-time equivalent faculty in Fall 1997	1,244.6	610.5	428.7	407.9
Traditional work hours	7 a.m. to 4 p.m. Monday to Friday	6 a.m. to 10:30 p.m. Monday to Saturday	Monday to Saturday	Not Specified
Minimum class size	15	Determined by Administration	Determined by Administration	20

All of the provisions agreed to by the district, when combined as a whole, may restrict the district's administrative flexibility and its ability to react to its fiscal crisis. As the table indicates, Los Angeles' faculty union agreement establishes a lower minimum class size, preventing the district from cancelling classes with 15 or more students. This policy differs markedly from those in other districts. By contrast, the San Francisco district established a minimum class size of 20 students, while the San Diego and Los Rios districts have no minimum class sizes in the faculty union contracts, leaving these decisions to management. Since Los Angeles' faculty is required to teach classes with as few as 15 students, the district's costs may be higher than those in other districts. For example, to teach 120 students who register in minimum-size classes, San Francisco has to fund six classes with the minimum number of 20 students, whereas Los Angeles has to support eight minimum-sized classes of 15 students.

Certain provisions of its union contract limit district flexibility:
- ✓ *Work weeks that restrict classes after hours or on weekends*
- ✓ *Extensive shared governance*
- ✓ *Addition of several advisory committees, some of which may be duplicative*

Another example of a union provision that limits the Los Angeles district's administrative flexibility is its shorter traditional faculty work week. The Los Angeles union agreement specifies that faculty have an eight-hour day, Monday through Friday. However, Los Rios and San Diego district faculties have to be available from Monday through Saturday. Further, Los Rios specifies that its faculty have to be available from 6 a.m. to 10:30 p.m. These longer hours give Los Rios and San Diego the freedom to schedule classes in the evenings or on Saturdays to accommodate working students. While Los Angeles can make a class assignment outside of the traditional work week, this departure requires the consent of the faculty member, an involuntary class assignment of a faculty member with the least seniority who must be informed in writing of the reasons for the assignment, or a search for a part-time instructor. Therefore, the district must take extra administrative steps to staff classes taught during nontraditional hours.

Finally, Los Angeles has agreed to extensive shared governance requirements beyond those required of community college districts by law. The California Education Code and state regulations require community college districts to involve students, staff, and faculty in some of their governance decisions. However, the Los Angeles district has agreed to additional shared governance provisions that include the creation of five committees, with union representation, at each of the nine colleges. We believe the administrative costs of convening such a large number of committees can be burdensome. Further, the district

agreed to let union representatives share in decisions that are more administrative than academic in nature, such as college and district budgets and affirmative action employment.

Moreover, some of the committees the faculty union agreement established appear to duplicate functions of existing committees. For example, the board's policy on shared governance already states that the board shall rely primarily on the district academic senate committee for curriculum matters, yet the union agreement requires the establishment of additional committees at the colleges that deal with curriculum. We question the need to use resources to duplicate work, especially when resources are severely limited.

Our concern is not with any of the individual provisions in the agreements. Instead, we question whether, taken together, these provisions are compatible with the district's need for administrative flexibility to reduce costs and adapt its programs to the needs of students.

INEFFECTIVE BUDGETING CONTRIBUTES TO OVERSPENDING AND DEPLETES DISTRICT RESERVES

The district has exercised poor budgetary control at all levels. Specifically, college officials have submitted to the central district office proposed budgets that fall far short of historical expenditures without having specific plans demonstrating how the colleges expect to operate within these budgets. The district office, despite noting some of these discrepancies, does not require college officials to make appropriate adjustments or prepare detailed plans before submitting the proposals to the board for approval. In addition, the district office has not controlled the colleges' expenditures during the year to ensure conformity with approved district spending plans. Rather, it has used reserves established at the beginning of the year to absorb overspending at the colleges. Finally, the board has approved district spending plans that include unrealistic or unsupported amounts for college activities and has not acted to preclude overspending during the year.

The Colleges Underbudget Certain Accounts

The district's budgeting practices are a major contributor to its fiscal difficulties. In attempting to submit a balanced budget, some colleges submit proposals that do not reflect historical

expenditures and underbudget for future expenditures. When the board approves a budget that clearly does not establish adequate resources for certain purposes or does not require colleges to explain the detailed steps they will take to make their operations more efficient, it allows crucial budgetary decisions to be postponed.

One college initially budgeted $26,000 in fiscal year 1997-98 for utilities that averaged $798,000 in the previous three years.

For example, in fiscal year 1997-98, one of the colleges initially budgeted a total of only $26,000 for several of its utility accounts, even though actual expenditures averaged $798,000 each of the three preceding years. The college eventually increased the budget to $93,000, but the actual expenditures amounted to $718,000. Thus, the college overspent its adjusted budget by $625,000. In another example from fiscal year 1997-98, one of the colleges budgeted only $357,000 for its utilities and housekeeping account, even though prior-year expenditures were $1 million. Instead of increasing its budget to a more realistic level, the college reduced the budget to $332,000. Actual expenditures amounted to $983,000, or $651,000 over its adjusted budget. We found a similar practice within the hourly teaching account. Colleges proposed budgets far lower than prior year costs, but did not identify or implement strategies to reduce costs. For example, in fiscal year 1997-98, one of the colleges only budgeted $1.5 million for hourly teaching, despite prior year expenditures totaling $4 million. The college's expenditures for hourly teaching in 1997-98 actually increased to $4.2 million.

The colleges have apparently used the utilities and the hourly teaching accounts as a means of submitting a balanced budget at the beginning of the year. Several of the presidents told us that some of the colleges typically underbudget the utilities account because if they exceed their budgets, the district office must step in to pay the bills, or risk having the utilities turned off, rendering the colleges inoperable. They also said that some of the colleges underbudget the hourly teaching account because there is a certain amount of discretion over the number of hourly teachers employed and, in a worst case scenario, the colleges could lay off the hourly teachers to cut costs. Given the overspending we have observed in the hourly teaching accounts, it appears the colleges have not consistently or adequately exercised this discretion.

On December 31, 1997, the district budget for salary costs in the unrestricted general fund was $221 million, $20 million less than the $241 million projected by the district on the same date.

The $20 million difference between the amount reflected in the budget and the total amount the district actually expected to spend on salaries contributed heavily to the projected $13 million deficit discussed previously in this report. Actual salary and benefit costs for the fiscal year totaled $240 million.

Underbudgeting or overspending certain accounts is an indication that many of the colleges are avoiding the difficult tasks of promptly identifying needed cost-cutting measures in other areas or pursuing other sources of revenue. Furthermore, budgets that do not reflect historical expenditures or are not based on practical plans to make operations more efficient detract from the usefulness of the budget as a critical tool for both guiding agency operations and ensuring that spending does not exceed revenues.

Unenforced Budgetary Controls Result in Use of Contingency Funds

The district has failed to enforce reasonable controls to prevent overspending.

Because the colleges have not adhered to their budgets, it is evident that the district has failed to enforce reasonable controls. Of the nine colleges, eight exceeded their budgets in fiscal year 1996-97 and six exceeded their budgets in 1997-98. Although according to the vice chancellor of operations the district's financial information system has controls to identify when the colleges will exceed their budgets, it appears that these controls have either been overridden or not implemented. We are concerned that, when the district office pays claims over the colleges' budgets, the colleges will feel encouraged to continue overspending.

To compensate for overspending, the district has imprudently used its contingency reserve account, which it funds with designated percentages of certain general fund revenues. According to the vice chancellor of operations, in the past, the district has utilized its reserves to cover the colleges' overspending. If the district continues using its contingency reserves to balance the budget, it may not have funds available for true emergencies. This practice further allows the district and colleges to avoid difficult budgetary decisions at the beginning of the fiscal year.

STATE LAW ALSO LIMITS THE DISTRICT'S ABILITY TO CUT INSTRUCTIONAL COSTS

Because it is required by state law to maintain a high percentage of full-time faculty, the district is limited in its ability to reduce its instructional costs. The Legislature passed Assembly Bill 1725 in 1988, which required community college districts to work toward a goal of having full-time faculty teach 75 percent of the instructional hours. The Legislature believed that full-time faculty would provide continuity to district curriculums and better services to the students. Since most districts statewide were below the 75 percent goal in 1988, the law initially required them to use a portion of their program improvement funds, and later, growth revenues, to increase their full-time faculty ratio every year until each district reached the 75 percent goal. If districts fell below the yearly percentage required by law, the state chancellor's office could fine them.

Since the fall of 1996, because the state chancellor's office thought that the district did not comply with this law, it has been negotiating with the district over the terms of the resulting penalty. In fact, the state chancellor's office withheld about $2.8 million from the district's apportionment in fiscal year 1997-98. However, in November 1998, the state chancellor's office determined that the district was not out of compliance and has proposed returning the amount it previously withheld.

The district believes it could reduce salary costs if it were able to hire more part-time, temporary instructors rather than maintaining as many full-time faculty.

Maintaining a high level of full-time faculty can be costly and can limit the district's ability to reduce costs to manage its fiscal crisis. The district states that if it had the option of hiring more part-time, temporary instructional staff, it would be able to reduce its salary costs because part-time instructors cost the district less than full-time faculty. The district believes that the financial burden of achieving and maintaining the 75 percent ratio is inequitable when the average full-time faculty ratio for community college districts statewide is 61 percent. Since part-time faculty members cost less, districts with a lower percentage of full-time faculty have lower salary costs in relation to their total expenditures.

THE DISTRICT HAS LACKED LONG-RANGE PLANNING

The costly decisions and poor budgeting controls we have discussed in this chapter have existed in an environment devoid of the benefits of adequate long-range planning. A meaningful

districtwide, long-range plan does not exist, nor do such plans exist for some of the district's individual colleges. Contributing to the lack of long-range planning is the recent high turnover rate for district chancellors—the district has had three different chancellors over the last three fiscal years—and, to a lesser extent, for presidents at some colleges. Frequent change in executive staff hinders developing and carrying out long-range plans. Although it has recently hired a legislative advocate to help address its long-range planning needs, the district's past practices of little long-term or strategic planning have deprived it of the benefit of a larger framework that defines its ultimate goals and identifies the processes for achieving those goals.

The district has been warned of the dangers of the lack of long-range planning before. In his message included in the district's report on the audited financial statements for June 30, 1997, the previous district chancellor stated that the lack of long-range planning had a significant, negative impact on the district's operations and financial condition. The Accrediting Commission for Community and Junior Colleges also cited the problem as contributing to the district's potential loss of accreditation status.

We believe that prudent long-range planning would benefit the district and the students it serves in the following ways:

- Improve the district's ability to anticipate and accommodate its future needs by identifying issues, opportunities, and problems it should address.

- Enhance decision making at both the operational and executive management levels to focus on results.

- Emphasize student satisfaction, especially if geared toward desired outcomes or benefits.

- Provide needed information to guide managers in making decisions about resource allocations and establish a basis for measuring the success of the district's activities.

Careful long-range planning might have helped the district avoid many of the mistakes it has made. ■

CHAPTER 2

Limited State and Local Funding Contributes to the Deteriorated Physical Condition of Facilities in the Los Angeles Community College District

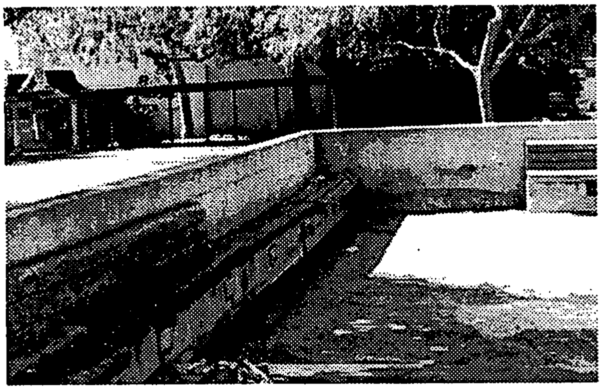
CHAPTER SUMMARY

Although there are differences in the appearance and age of the nine campuses, all of the colleges at the Los Angeles Community College District (district) clearly have facility needs that remain unmet, and some areas of the campuses are run down and in need of repairs. Limited state and local funding for capital outlay, scheduled maintenance, and routine maintenance hinders the district from constructing new facilities and maintaining existing ones. The district could strengthen its planning for the future to ensure that its greatest facility needs are met and that decision makers remain aware of those needs remaining unmet.

BACKGROUND

The Chancellor's Office of the California Community Colleges (state chancellor's office) implements and enforces rules and regulations for the allocation of funds authorized under the State's capital outlay and scheduled maintenance programs. Generally, projects with an estimated cost of $400,000 or more are classified as capital outlay which, if approved, receive 100 percent funding from the State; however, projects costing between $10,000 and $400,000 are eligible for funding through the scheduled maintenance program. Funding for approved scheduled maintenance projects is generally shared equally between the State and districts. Because districts rely heavily on these programs, lack of funding statewide may contribute to the slow degradation of the college facilities and infrastructure.

We visited all nine campuses in the district and observed many examples of facilities and grounds in need of repair. From the exterior, we noted cracked walls; chipped building facades; many


Damaged and unkempt student rest area at Harbor College.

temporary classrooms; potholes in parking lots and roads; and untrimmed trees, shrubs, and grass. On the inside of some buildings, we noted missing ceiling tiles, a damaged stairwell, buckled floor tiles, evidence of leaky roofs, and no air conditioning. While we did not note any situations that posed serious and immediate health and safety risks, we believe that the physical condition is poor enough to cause potential students to consider attending another school.

STATE FUNDING FOR CAPITAL OUTLAY PROJECTS HAS NOT KEPT PACE WITH THE NEEDS OF COMMUNITY COLLEGES

Many community college districts throughout the State, including Los Angeles, have been unable to progress with needed capital outlay projects because state funding has been so limited. Their needs far exceed the available state resources to fund them. In fact, as of July 1998, five-year construction plans already submitted to the State by community college districts contain a backlog of projects estimated to cost over $4 billion, according to the state chancellor's office. This backlog includes projects totaling $1.8 billion the state chancellor's office has approved but not yet funded.

Community college districts' five-year construction plans show a backlog of projects expected to cost over $4 billion.

In making decisions about which projects to fund, the state chancellor's office generally follows the priorities specified on the following page. The State first funds any new or incomplete phases of Category A projects. If dollars remain, the State next funds incomplete phases of approved Category B and C projects. The State allocates any leftover dollars to new Category B and C projects in a ratio of 80 percent to 20 percent, respectively. While projects in all the categories are eligible for funding, due to limited state resources, the priority of the state chancellor's office is funding projects to meet safety requirements. For the fiscal years 1996-97 through 1998-99, the state chancellor's office has only accepted proposals for new projects in Category A, the first two project types under Category B, and the first project type in Category C. Furthermore, the office deleted A-4 as a priority category; it will not consider proposals for this category until further notice.

Criteria Used by the State Chancellor's Office to Prioritize State Capital Outlay Funding

Category A. To activate existing space.

*1. Safety requirements, correction of hazardous conditions, and basic access for disabled persons.

*2. Equipment for previously funded projects.

*3. Replacement or alterations to infrastructure when failure or loss would otherwise result.

4. Alterations, renovation, or remodeling necessitated by previously funded projects.

Category B. To provide new space or remodel existing space for instruction, and for academic and administrative support facilities.

*1. Master plans and preliminary plans when major deficiencies exist and it is projected that the district will receive capital outlay funding within five years.

*2. Remodeling and new construction of classrooms, teaching laboratories, libraries, and learning resource centers.

3. Remodeling and new construction of academic and administrative support facilities.

Category C. To provide for other capital outlay projects and promote a complete campus concept.

*1. Physical education, performing arts, and child care and development facilities.

2. Cafeterias, maintenance shops, warehouses, other support facilities, and energy conservation projects.

3. Other capital outlay projects that promote a complete campus concept.

4. Renewal and improvement of existing instructional and support facilities.

Source: *The Capital Outlay Handbook for the California Community Colleges, November 1997.*

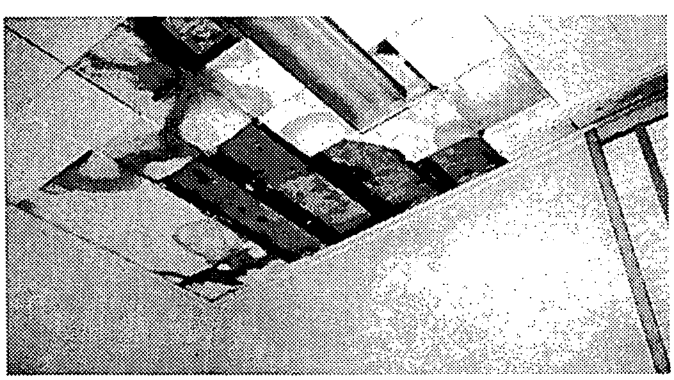
* The State agreed to fund new projects only in these categories in fiscal years 1996-97, 1997-98, and 1998-99.

The State Budget Act of 1998-99 allocates $205 million in funding for 44 capital outlay projects throughout the State's community college system. Three of the 44 are new projects and the remaining 41 are continuing projects in various categories. Of the dollars awarded in fiscal year 1998-99, the Los Angeles district received $269,000, less than 1 percent of the total, to fund only one continuing Category A-2 project. According to the district's assistant director of facilities planning and development, projects the district requested that were not funded in fiscal year 1998-99 included installation of a new ventilation system, a new fire alarm system, and construction of a student services center.

In November 1998, California voters approved a $9.2 billion public education bond measure, which provides $2.5 billion for construction of facilities at institutions of higher education, including community colleges. While this measure will provide some relief to community colleges, the funds will not be sufficient to address the $4 billion backlog of projects the state chancellor's office identified in the districts' five-year construction plans. In addition, the community colleges must share the $2.5 billion in funding with the California State University and University of California systems.

INSUFFICIENT STATE AND LOCAL FUNDS EXIST TO ADDRESS MAINTENANCE NEEDS

The lack of funding for needed capital outlay projects may also negatively affect the scheduled maintenance program. Due to the lack of sufficient capital outlay funds and the restrictions imposed on the types of projects considered for funding, the state chancellor's office has suggested that districts split capital outlay projects into smaller phases that may qualify for funding under the State's scheduled maintenance program. Scheduled maintenance needs already exceed available funding, so this practice creates additional competition for these limited resources. In addition, the financial commitment of the community colleges for such projects increases because, while the State pays 100 percent of the costs of



Leaky roof and damaged ceiling tiles at City College.

approved capital outlay projects, the scheduled maintenance program generally requires the colleges to pay half of project costs.

The purpose of the State's scheduled maintenance program is to fund projects for unusual and nonrecurring work that restore a facility to a safe and continually usable condition. Unlike the capital outlay program, scheduled maintenance projects require local matching funds generally equal to the amount of state funds allocated for the projects. However, depending on the financial condition of the district, the state chancellor's office may partially waive the matching requirement.

Funding from the State's scheduled maintenance program also has not kept pace with districts' needs throughout the State. For example, the state chancellor's office reports that, of the $180 million in requests for scheduled maintenance projects all community college districts submitted for the 1996-97 fiscal year, it only funded projects valued at $127 million. The remaining unfunded projects, valued at $53 million, were rolled forward for consideration in the 1997-98 fiscal year. Similarly, in fiscal year 1997-98, the state chancellor's office reported funding $100 million worth of projects, even though districts submitted requests for projects valued at $179 million.

In fiscal year 1998-99, the state chancellor's office approved only $8.7 million in scheduled maintenance projects for the Los Angeles district, $19.5 million less than it requested.

The Los Angeles district has had the same lack of success for state funding as other districts. In fiscal year 1997-98, the district requested about $23 million in scheduled maintenance projects, but only about $10 million was initially approved. In fiscal year 1998-99, the state chancellor's office initially approved only $8.7 million in scheduled maintenance projects, which was $19.5 million less than the district requested. Further, as discussed in the next section, the value of projects ultimately funded was even less than those initially approved.

Inability to Match State Funding Results in the District Terminating Some Projects, and Delays in Completion Put Additional Projects at Risk

The district's inability to match state funding for approved projects has reduced the number of projects it can complete under the State's scheduled maintenance program. If it is unable to fully match state funds with an equal amount of local funds, a district may request a waiver from the state chancellor's office to reduce the matching requirement. The decision to waive a

portion of the match is based on the district's balances in its unrestricted general fund as reported in its financial statements at the end of the preceding year. Nevertheless, this waiver does not reduce the amount of state funding the state chancellor's office agreed to provide. Rather than starting all of the approved projects without enough funds for completion, the district must reduce the number of projects. For example, assuming the State approved $100,000 worth of projects, the State and district would generally contribute $50,000 each to fund the work. However, if the district could only afford $30,000 and the State granted a waiver, the district would have to eliminate a sufficient number of projects to bring the total cost down to $80,000. Although districts can resubmit projects deleted in one year during the subsequent year, beginning in fiscal year 1996-97, districts that either allow a significant amount of their grants to revert, or are granted waivers, may receive less consideration for funding future projects.

For fiscal years 1996-97 through 1998-99, the district was unable to meet its full matching requirement under the State's scheduled maintenance program. The state chancellor's office granted partial waivers each year, which resulted in the elimination of more than $12 million in state-approved projects over the three years, as shown in Table 3.

TABLE 3

District Scheduled Maintenance Projects by Fiscal Year (In Millions)

Year	Cost of Projects Initially Approved	Cost of Projects Funded	Amounts of Projects Cancelled
1996-97	$21.3	$13.7	$7.6
1997-98	9.8	7.7	2.1
1998-99	8.7	6.2	2.5
Total	$39.8	$27.6	$12.2

Source: District and state chancellor's office project listings.

The district's inability to pay its full share of approved scheduled maintenance projects further hinders its ability to complete needed maintenance projects.

Because of delays in project completion, the district may risk losing scheduled maintenance funding for projects approved in fiscal year 1996-97. In March 1997, the state chancellor's office entered into an agreement with the district to fund 109 scheduled maintenance projects valued at $13.7 million. The State is to pay $10.6 million (78 percent) of the approved project costs, while the district is to provide $3 million (22 percent). Since the state chancellor's office has indicated that it does not allow deadline extensions, the district must complete all projects by May 1999 to receive the full share of state funding. Records from the district's facilities planning and development unit show that, as of September 1998, the district had completed only 16 of the 109 projects. In addition, 24 of the remaining 93 projects were still in the design stage. According to the district's vice chancellor of operations, with the addition of three facilities staff in the past year and plans to hire another, the district expects to have contracts in place for all of the projects soon.

Vacant Maintenance Positions May Contribute to the Poor Appearance of Facilities

As of October 1998, the nine colleges had at least 68 unfilled maintenance and operations positions, a 15 percent vacancy rate.

The district could improve the physical appearance of its campuses and better maintain its facilities by filling currently vacant maintenance and operations positions. As of October 1998, we found at least 68 unfilled maintenance and operations positions at the nine campuses, based on budgeted positions in the 1998-99 final budget. This represents a 15 percent vacancy rate. One campus has a 57 percent vacancy rate, with only 12 of 28 budgeted positions filled. Positions we considered as maintenance and operations included custodians, gardeners and groundskeepers, painters, electricians, carpenters, plumbers, heating and air conditioning staff, and maintenance assistants. Some colleges indicated that they have not been able to fully fund their routine maintenance needs because of fiscal difficulties. However, we are concerned that if the colleges continue to neglect routine maintenance, the condition of facilities could deteriorate further and be more expensive to address in the long run.

THE DISTRICT COULD IMPROVE ITS CAPITAL OUTLAY AND SCHEDULED MAINTENANCE PLANNING

As noted above, state funding for capital outlay and scheduled maintenance projects is scarce and, overall, the district has requested more projects than have been approved. However, we found that the district could improve its chances for funding by being more proactive in its capital outlay planning and by better tailoring its requests for scheduled maintenance projects to state priorities. For example, three campuses have not requested capital outlay funding in fiscal year 1998-99, even though they have unmet needs. In addition, three of the four campuses at which we evaluated capital outlay planning do not have updated facilities master plans, although if they request capital outlay funding, they must describe how each project they propose supports the campus and district master plans. One of the college presidents we spoke to about capital outlay planning indicated that historically, he has requested a minimal number of capital projects because his college's needs have not matched the State's criteria regarding eligible projects. However, in our view, the college presidents must continue communicating their capital outlay needs to the board and the State so that these key decision makers are aware of unmet needs and can pursue alternatives to address the problems.

If the district is unable to address unmet maintenance needs, facilities could deteriorate further and become unsafe.

Furthermore, the district's method for prioritizing its scheduled maintenance projects is at odds with the State's method. The State prioritizes projects by category in the order that follows: roofs, utilities, mechanical equipment, exteriors of buildings, and other projects. In order to allow each college an opportunity to receive some scheduled maintenance funding, the district establishes its priority list by selecting one project from each college in alphabetical order, followed by a second round of choices in reverse alphabetical order. While this method appears equitable, it causes the district to request projects of lesser state priority before those of higher state priority. For example, for fiscal year 1998-99, the district ranked replacement of a gym floor and a stage floor, which fall in the State's lowest-priority "other" category, as priorities 17 and 24, respectively. Meanwhile, it ranked four roof replacement projects, which fall under the State's first category, as priorities 53, 56, 71, and 74. While the state chancellor's office reevaluates a district's project priorities to determine which projects the State will fund, the district could likely improve its chances for funding by presenting its needs in a manner consistent with the State's funding priorities.

The district's unmet facilities needs are great, and the lack of funding at the state and local levels creates a significant challenge for the district to overcome. If it is unable to find ways to address these unmet needs, facilities could deteriorate even further and become unsafe, resulting in hazards to faculty, staff, and students. These conditions may also contribute to lower enrollments, which the district can ill afford because that would reduce its revenues and further erode its fiscal condition. ■

CHAPTER 3

Current Reforms Have Yet to Resolve the District's Fiscal Problems and Will Create New Challenges

CHAPTER SUMMARY

Although the district's current reforms began in response to its fiscal crisis, the early stages of its reform plans do not sufficiently address those conditions that have historically contributed to its financial problems. Further, one aspect of proposed reforms, decentralizing administration, creates a new set of challenges for the district. Because the reforms have just begun, we do not expect the district to have fully addressed each of these issues. However, we believe it should have fully assessed the benefits and drawbacks of decentralization before moving in this direction, and then should have established more specific objectives and actions to reach its goals. Until the district deals with all of these matters, its fiscal problems will remain.

THE DISTRICT'S REFORMS ARE PROGRESSING GRADUALLY

The district launched its current reform efforts in an attempt to move beyond crisis management and address the systemic causes of its problems. According to the president of the board of trustees (board), for many years the district has dealt with immediate crises, but has then continued to operate as usual. When the district's immediate crisis in fiscal year 1997-98—the projected $13.2 million deficit in the unrestricted general fund —was resolved, the board recognized that the district's problems were systemic, initiated reforms, and publicly committed to ensuring their implementation.

The board voted in April 1998 to decentralize the district's operations by July 1, 1998, or as soon as legally possible thereafter, yet, as of October 1998, the district was only in the early stages of planning for decentralization.

This chapter assesses the district's steps toward reform to date, and the extent to which they address the historical problems discussed earlier. We also provide some cautionary comments that we believe the district must consider when deciding how and to what extent it will decentralize.

ALTHOUGH THE DISTRICT HAS BEGUN REFORMS, IT HAS NOT YET FULLY ADDRESSED ITS HISTORICAL PROBLEMS

Reforms the Board Approved

1. To tie college funding directly to performance, allow each college to retain the revenue it generates. This reform would be phased in. In previous years, the district based budgetary allocations to colleges primarily on their prior-year expenditures.
2. Include items previously reflected in the districtwide accounts in the college budgets to the extent possible.
3. Allow each college, through consultation with its academic senate, to determine its academic requirements and curriculum.
4. Allow colleges to determine, based on their needs, the services they perform and the services they want the district office to perform.
5. Develop a process by which the colleges pay for the services performed centrally and for a prudent districtwide reserve. The colleges would also maintain a prudent college reserve.
6. Hold the college presidents directly accountable to the district chancellor and the board.
7. Subject implementation of the plan to board approval.

Through its reforms, the district has begun to address some of its historical fiscal problems. As we discussed in Chapter 1, the district has had problematic budgeting practices, with inadequate fiscal controls, that resulted in overspending. In addition, we identified increasing and excessive costs that contribute to the district's fiscal troubles. Further, while reforms appear to increase the responsibility and role of college presidents, district- and state-imposed requirements may impede their efforts to effectively control spending and manage budgets. The district needs to make additional changes in these areas that its reform efforts have yet to fully address.

The District Has Begun Making Some Positive Reforms

The district has initiated some positive reforms that could result in significant operational improvements. For example, the board is implementing plans to more carefully scrutinize and monitor each college to ensure that it operates within budget. It requires the colleges and the district office to prepare a quarterly report to include annual projected expenditures and identify steps necessary to maintain a balanced budget. According to its president, the board has appointed an advisory committee comprised of three presidents from the most successful colleges. The advisory committee is tasked to continually provide the board with reports on the viability and progress of colleges' plans for balancing their budgets. The board president has also

indicated that the district intends to develop improved computer systems that will provide more timely and accurate tracking of expenditures and will include controls to prevent overspending. Additionally, at least one of the colleges has warned its employees of their personal liability for entering into inappropriate payment obligations, such as arranging for purchases, contracts, or leases without an authorized purchasing document, or assigning personnel to work without proper authorization. Moreover, it specifies that no one should accept gratuities from any vendors doing business with the college. While each one of these reforms could and should be in place just as easily in a centralized administration, we believe each represents a step in the right direction to address abusive practices. However, the district still needs additional changes to avoid overspending, as we discuss in the following sections.

The District's Efforts to Improve Its Budgetary Process May Not Be Adequate

To help prevent the past practices of unrealistic budgeting and overspending of campus budgets, the board has stated that it will hold campus presidents directly responsible for operating within their budgets. It plans to remove any president who fails to keep spending at or below allocated amounts. The district has directed its administrators and staff to work with the presidents to plan how they will increase revenues and decrease expenditures. To monitor progress for each campus, the board has begun reviewing each campus president's fiscal plans and progress toward operating within budget. Although we believe the board's careful scrutiny is essential for fiscal accountability, the day-to-day controls at the college and district level are also necessary. Moreover, we have concerns related to the implementation of this policy.

Despite some operational reforms, the board has continued to allow colleges to submit unrealistic budgets that could result in further overspending.

First, the board repeated its mistake of prior years by approving a final budget for the 1998-99 fiscal year that, while it was balanced, was either not realistic or was not accompanied by specific plans to ensure compliance with the budget. In September 1998, the district office predicted a $7.2 million shortfall in the unrestricted general fund for the year for certain campuses and its own operations. As of October 1998, we had not seen any firm plans indicating how the district will address this projected shortfall.

Thus, the board has continued to allow important budget decisions to be delayed. For example, one of the colleges budgeted only $2.7 million for its hourly teaching account, despite prior-year expenditures of $5.8 million. Two weeks after the board approved the final budget, another college indicated it had underbudgeted by $700,000, then proposed cuts in expenditures. As we discussed earlier, the board president charged the advisory committee with monitoring college spending plans and providing feedback to the board. However, we believe that the board should consider whether budgets are sufficient and require colleges to identify appropriate actions to reduce costs or increase revenues, if necessary, prior to approving the colleges' final budgets.

Colleges have established "holding accounts" to attempt to cover budgetary shortfalls.

Both of the presidents with whom we discussed underbudgeting of accounts in the 1998-99 final budget explained that the colleges have set aside a portion of their district allocations for "holding accounts" to adjust the budgets and reserve funds as needed. The holding accounts appear to be new for the colleges this year, with seven of the nine colleges budgeting more than $500,000 each in such accounts. We question whether these accounts will adequately cover all instances of underbudgeting or inadequate cost-cutting. Should the resources prove inadequate, the delay in reaching crucial decisions could have results similar to those in fiscal year 1997-98, when the colleges had less than six months to reduce expenditures and increase revenues. If the colleges address their budget problems more promptly, they have the opportunity to spread the effect of anticipated shortfalls over a longer period, making the impact of the cuts more gradual. In addition, early recognition of potential shortfalls allows the board and the colleges more time to explore alternative solutions.

To prepare for negotiating contracts and to assess the effectiveness of college presidents regarding budgetary controls, the board met with the college presidents to discuss their budgetary plans on September 23, 1998, two weeks after it approved the final budget. Because these discussions took place in closed session, it is not entirely clear to us how complete the presidents' plans submitted for board scrutiny are, or how thorough the board's review is. Based on the six handouts for these meetings we have seen, the amount of detail the presidents submit can vary widely, ranging from a single page, listing five vague proposals to reduce expenditures, to a lengthy document specifying numerous anticipated costs and steps to reduce them. We

believe that, in seeking the rationale for the presidents' budget proposals, the following questions are just a few examples of what is reasonable for the board to ask:

- Is each major budget category reasonable when compared to prior-year expenditures, and, if not, what is the basis for the change?
- If budgets are cut or enhanced significantly, what practical changes in number of staff, types of services, or purchase of goods are the presidents proposing to justify the budget changes?
- Have the campuses made efforts to enhance revenues through grants or agreements with private enterprises?

Each of these questions would require a specific plan of action for the colleges to operate within realistic budgets.

Reforms Have Not Yet Brought About Anticipated Cost Savings

It is not clear that decentralization efforts will result in significant cost reductions.

Part of the impetus behind the district's decision to begin decentralization reforms was the need to address its financial problems. With decentralization, the district anticipated increased efficiencies by eliminating duplicate functions and streamlining current processes. However, as the discussions of reform have progressed, we have seen little evidence that the district has actually achieved anticipated cost reductions. Instead, much of the discussion has focused on questions over the district administration's authority to make decisions or approve actions. For example, numerous committees are meeting to propose which district office activities can be decentralized and performed at the college level. The committees consider how many district staff perform certain functions and how practical it is to divide these staff among the various campuses; nevertheless, we have not yet found that the committees have identified opportunities for significant cost reductions. It is also not clear that housing staff at the colleges instead of the district office would save money, especially if the staff would require new equipment or additional space.

When we asked for the board's perspective on the fiscal impact of its reforms, the board president indicated that the district has projected some of the possible fiscal impacts of the reforms and some of the positions to be eliminated. She also indicated that

the reforms are a dynamic, ongoing process and it is impossible to project all the eventual fiscal impacts. We agree with her comments. Further, we believe that by continuing systemic reforms of its administrative and budgetary practices, the district may ultimately ensure that colleges operate within realistic budgets. However, we reiterate that the district anticipated from decentralization a significant reduction in costs, which has not yet materialized.

While Making College Presidents More Accountable, Reforms Do Not Adequately Address District- and State-Level Decisions That Remain Outside the Presidents' Control

The reform has not yet sufficiently addressed the effect of districtwide decisions on individual colleges and their presidents' ability to succeed under decentralization. While reforms hold the presidents responsible for college budgets and deficits, some major decisions affecting those budgets currently remain at the state or district level. Thus, presidents may have responsibilities that are not commensurate with their authority.

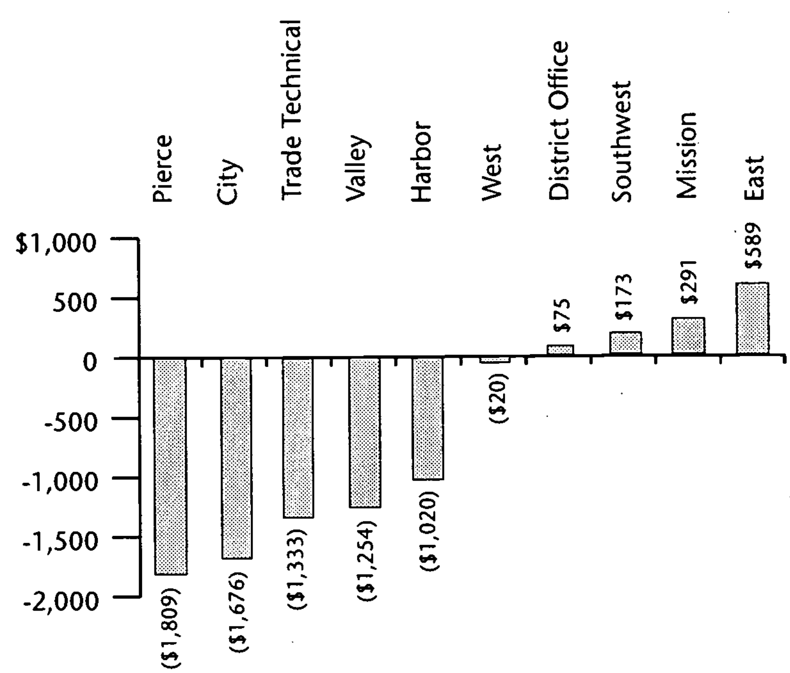
College presidents face the difficult task of operating within budgets over which they have little control.

For example, salaries and benefits have accounted for 85 percent of unrestricted general fund expenditures in recent years. Under decentralization, budgets for the individual colleges incorporate these costs, and the presidents must ensure that they operate within these budgets. However, districtwide agreements with unions could again increase salary costs by stipulating wage increases or reducing the minimum work week for faculty. As we noted in Chapter 1, other factors also limit the presidents' options in dealing with salary costs, including the district's expressed intent to avoid layoffs whenever possible; the State's requirement that 75 percent of student-contact hours be with full-time faculty, which limits options for using less expensive part-time faculty; and the minimum class size of 15 established in the districtwide faculty union contract, which precludes the presidents from eliminating those classes with low enrollment.

Thus, the college presidents face the difficult task of operating within their budget allocations although their budgets include significant expenditures over which they have very limited control. As Figure 3 on the following page illustrates, district data indicate that six of the nine college campuses reported operating deficits for fiscal year 1997-98.

FIGURE 3

Six Colleges Overspent Their Budgets in Fiscal Year 1997-98 (In Thousands)



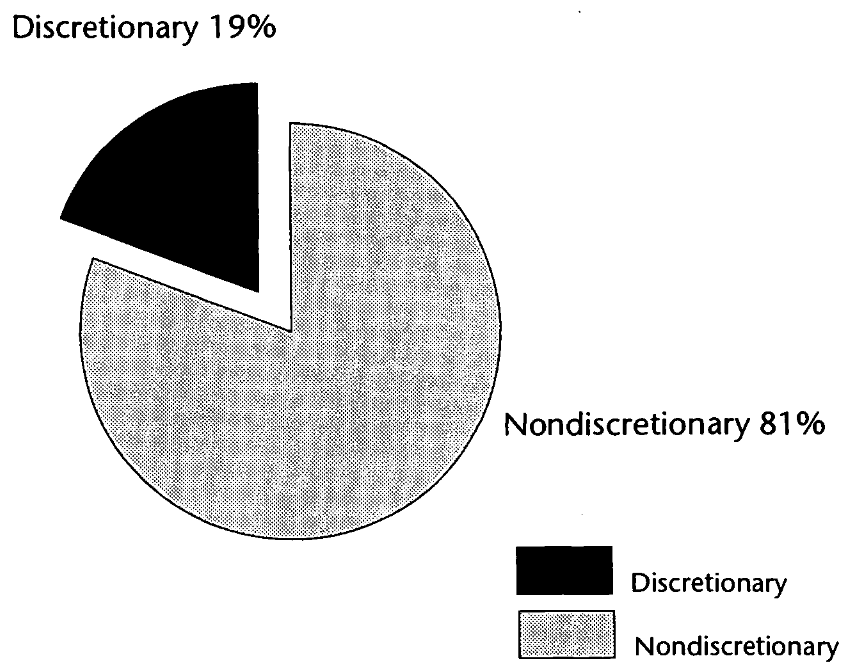
Source: Los Angeles Community College District final budget document for 1998-99.

One of these campuses, Valley College, further illustrates the financial dilemma some presidents may encounter. For the 1997-98 fiscal year, Valley College reported an operating deficit of $1.3 million, almost 4 percent of its total $32 million budget allocation from the unrestricted general fund for the 1998-99 fiscal year. We estimate the president has discretionary control over only $6.1 million of its $32 million budget, as Figure 4 on the following page indicates.

The president has little control over 81 percent of the budget, which, except for about $300,000 for utilities and housekeeping expenses, is for non-certificated and regular certificated salaries and benefits. We categorized hourly salaries of $1.4 million as discretionary, even though the president has no control over the rate of pay, because she controls class scheduling and the use of regular faculty, which determine how many hourly teachers the college needs. In addition, $3.4 million of the $6.1 million we view as discretionary is the amount Valley College has set aside in a "holding account," described earlier in the chapter. How-

FIGURE 4

Valley College Has Limited Control Over Its Unrestricted General Fund Budget



Source: Derived from data in the Los Angeles Community College District final budget document for 1998-99.

ever, to the extent it does not create efficiencies elsewhere, we believe the college will need to use some of this reserve to cover costs beyond its current budget in its hourly teaching and utilities and housekeeping accounts. In particular, we expect the college will have to use part of the holding account for utilities and housekeeping, currently budgeted at an impossibly low amount of 31 percent of the actual costs for fiscal year 1997-98.

To solve short-term budget shortfalls, some colleges have received financial assistance from other colleges. This assistance from the "have" colleges to the "have-not" colleges is a temporary district measure, to be phased out over a three-year period beginning in fiscal year 1998-99. It is intended to give the "have-not" colleges an opportunity to gradually implement cost-cutting and revenue-enhancing measures over that period. The board also relieved those colleges with operating deficits in prior years of the need to repay the district for the amounts that they overspent.

When we asked the board how it planned to hold college presidents accountable when they had little control over significant portions of their colleges' expenditures, in particular salaries, the board president responded that the presidents are now significantly involved in salary negotiations and the board would give "important consideration to recommendations of the presidents," even though the final decisions remained with the board. We believe the presidents' close involvement in decision making is essential, and the board is well-advised to respect the needs of all district constituencies. Before taking action, the board should carefully consider whether its decisions impede the presidents' ability to control spending and whether resources are sufficient to cover board decisions that increase costs.

The presidents face an imposing, but not an impossible, task. In our opinion, ensuring that colleges operate within their budgets will require a coordinated effort involving the college presidents, the district office, the board, the academic senates, and the unions. This effort will require development of strategies to maximize resources and cut down on inefficiencies. All levels must be willing to make difficult decisions for the benefit of the district as a whole and must acknowledge that their decisions may have repercussions at other levels.

DECENTRALIZATION CAUSES ADDITIONAL CHALLENGES

As the district decentralizes, it will face additional challenges that deal with changes in the lines of responsibility, increased competition between campuses, and quality of education. Because decentralization reforms have just begun, we neither expected, nor found, that the district has fully addressed each of these challenges. However, we believe it is reasonable to expect the district to begin with a good long-range plan for decentralization that addresses these issues as part of an overall framework. The plan should consider the primary goals of decentralization and how the district plans to reach its goals; however, it does not yet have such a plan.

The District Does Not Yet Have a Long-Range Plan for Decentralization and Its Ultimate Effects

The district has chosen to decentralize without defining its ultimate goals and determining how best to achieve those goals. Without such a long-range framework within which to make decisions, the district runs the risk of making those decisions in isolation and on an "as-needed" basis. Such decisions can have unintended results.

As we indicated in Chapter 1, the benefits of long-range planning make such efforts critical. Long-range planning is a future-oriented process of assessment, goal setting, and decision making that maps an explicit path between the present and a vision of the future.

Essential Steps in Long-Range Planning

- Analyze work environment to identify strengths, weaknesses, problems, and opportunities.
- Identify the key issues relating to the mission and planned activities.
- Define the mission and formulate consistent goals.
- Establish priorities among the goals and allocate resources accordingly.
- Define the objectives necessary to achieve each stated goal.
- Establish time lines and action plans to complete each objective.
- Define benchmarks or targets for each significant activity.
- Measure the results of operations against the benchmarks to evaluate performance and reset targets as necessary.

Successful long-range planning would focus the district on defining the type of organization it wants to become, developing its goals, and establishing its priorities.

Although the board voted to decentralize the district administration in April 1998, it does not yet have a long-range plan for the process, nor has it articulated a clear vision of the end result it wants to achieve from the current reforms. As we indicated in Chapter 1, the district has hired a legislative advocate, in part to help with long-range planning. However, the legislative advocate has other responsibilities, including lobbying duties that require his presence in Sacramento for at least part of the year. Thus, his availability for long-range planning may be limited.

As of October 1998, the presidents had not submitted a detailed proposal for decentralization for the board's approval. In fact, the presidents have recently reported to the board that "concentrated and focused efforts toward continued reform and decentralization will be required for several years to come because [the district is] seeking fundamental yet intricate changes in a large, complex organization." We believe it is appropriate for the

district to fully examine the consequences of any proposed steps toward decentralization, but it also needs a clear vision of expected results.

The District Has Yet to Determine Revised Areas of Responsibility

While reforms are not complete, they have not yet resulted in adequate policies and procedures that clarify who is responsible for which activities and to what extent. As part of the process of preparing for decentralization, the district office has started to determine which responsibilities it is statutorily obligated to meet. The district as a whole has certain obligations determined by statute or practical necessity that require the use of a district forum.

The colleges must identify and hold accountable individuals responsible for budgetary control.

The district will have to describe the system of internal controls it envisions and whether each of those controls will be at the district level, at the college level, or shared. The district or each of the colleges will then have to draft new procedure manuals reflecting changes in policy. For example, if individual colleges must operate within their budgets, each must ensure that it clearly identifies what position or function on campus will guarantee that sufficient budgetary authority exists to make each payment requested. Will this responsibility reside with accounting technicians, accounting officers, department chairs, the college president, or some other individual? Will the responsibility be split, depending on the nature and size of the expenditure? If reforms do not create clear policies to effectively define responsibilities and establish procedures to hold designated individuals accountable, staff will have less incentive to act responsibly. For instance, if it is not part of his or her stated responsibilities, the accounting technician who receives a check request for a computer purchase may prepare the check without even recognizing the need to determine whether a sufficient balance exists in the budget to cover the purchase. The accounting officer who reviews and authorizes the payment may assume that the accounting technician has ensured the budget is sufficient. Thus, the check could be paid even though the budget has been exhausted.

The District Has Not Addressed the Issue of Competition Among Colleges

The reform plan does not yet include a district strategy for dealing with competition among the colleges. We believe the move toward decentralization—assigning personal responsibility for the budget to each college president and allocating funds based partially on enrollment—has the potential to increase intercollege competition for students. Without a plan for dealing with the effects of competition, the district may be unprepared to take action to assist a campus that does poorly or fails. It is conceivable that a college effective in teaching students could fail because its location, target population, physical plant age, or type of programs make it more expensive to operate. A "failing" college might have to depend on competitor colleges for emergency assistance.

When we asked for the board's perspective on whether and how the survival of each college would be ensured in a competitive environment, the board president responded that colleges play an important role in creating their own success through innovative programs, scheduling, and marketing. The board believes each college has the ability to be successful, and success is best accomplished by providing autonomy to the colleges and rewarding them for their endeavors. The president indicated further that the board is committed to ensuring the continuation and success of each college and will take appropriate measures to assist the colleges.

In the short term, colleges with more resources will continue subsidizing those with fewer resources. In the longer term, at least one college will have difficulty operating without subsidies.

In the short term, colleges with more resources compared to expenditures are subsidizing those with less. As Table 4 on the next page indicates, this temporary assistance to struggling colleges results in the larger colleges subsidizing smaller ones, with a significant subsidy for one college in particular. Southwest College will receive a subsidy of over $660 in fiscal year 1998-99 for each full-time equivalent student (FTES) on its campus. This represents almost 15 percent of the college's total allocation per FTES.

TABLE 4

Larger Colleges Subsidize Smaller Colleges

Colleges	Full-Time Equivalent Students	Impact of Subsidy on Allocation per Full-Time Equivalent Student Amount ($)	Percentage (%)
East	11,787	($170)	(5.3)%
City	10,155	(93)	(2.8)
Valley	10,042	(127)	(4.0)
Trade Technical	9,798	(56)	(1.7)
Pierce	8,721	197	5.6
Harbor	5,247	136	3.7
West	4,799	21	0.6
Mission	3,635	52	1.4
Southwest	3,510	663	14.9

Source: Los Angeles Community College District final budget document for 1998-99.

Note: Parentheses indicate subsidies provided.

However, the board's plan is to phase out these subsidies over three years. Increasing revenues and decreasing costs to compensate for the loss of this substantial assistance will be very difficult for Southwest College, and we question its ability to operate within its budget without subsidies in three years, even with the best of intentions and the most aggressive plan for improvement and growth. Its difficulties could be exacerbated by the increased competition from the other district colleges. On the other hand, should the district opt to continue subsidies for struggling colleges, it could provide a disincentive for others to perform well: their allocations would be reduced to assist the struggling colleges.

The Need for Financial Solvency May Affect What Educational Services a College Offers

By allowing each campus to determine its course offerings and schedule, decentralization may provide them the opportunity to adapt more readily to student needs. Curriculum decisions will no longer require district approval. However, decentralized decision-making and a focus on the bottom line create the

possibility that campuses will eliminate important, but expensive, classes. For example, vocational education laboratory classes require more expensive equipment and often accommodate fewer students per class. Although the district has supported such classes, an individual campus under financial duress may not. In fact, faced with a potential deficit of $1.2 million in fiscal year 1998-99, West Los Angeles College has proposed eliminating the portion of its 1999 summer school program that the fiscal year 1998-99 budget would fund. While we recognize that cancellation of programs may sometimes be necessary during periods of fiscal difficulty, these decisions need to be balanced from a districtwide perspective.

In an effort to cut costs, one college has proposed eliminating part of its summer school program.

THE ULTIMATE IMPACT OF PROPOSED REFORMS ON THE DISTRICT IS NOT YET CLEAR

We have discussed only some of the questions the district must address in deciding how far it should go with decentralization, such as where to place important controls, how much autonomy to grant to individual colleges, and what the role of the district office should be. Currently, without the general philosophical guidelines and more explicit goals and procedures that long-range planning can offer, the district runs the risk of making decisions with unintended consequences. For example, decentralization could ultimately lead to each college functioning as a separate district. While we do not believe the district intends to split up, some of the steps toward decentralization encourage each college to look out for its own interests. When does this trend become counterproductive to the good of the district as a whole? When does the district become a loose confederation of colleges or nine independently operated entities? Although, in our opinion, the district inappropriately rushed its decision to decentralize without thoroughly examining the benefits and drawbacks, it has since slowed to a more deliberate process. It must now continue the process of promptly, but carefully, establishing its ultimate goals and determining how—and whether—it can achieve them with decentralization. ■

CHAPTER 4

Conclusion and Recommendations

The district is experiencing a fiscal crisis brought on largely by costly management decisions, ineffective budgeting practices, and the lack of long-range planning. The physical condition of many campus facilities is poor, and neither the State nor the district is providing sufficient funding to adequately improve and maintain them. Further, although still in the early stages, the district's reform efforts have not adequately dealt with its historical fiscal problems. The reforms create additional challenges the district will need to address as well.

RECOMMENDATIONS

The district's board of trustees (board) should ensure the development of district- and college-level long-range plans to provide a cohesive framework on which to base significant decisions in the future. This long-range planning should define the district's direction and should address the following:

- Before approving any salary increases, the district should ensure that it has adequate funds to cover them. Moreover, the district should evaluate the level of resources it commits for classified staff in light of expenditures it incurs for certificated salaries.

- To ensure that the district does not incur expenditures for unused space, it should try to lease vacant space currently available at the district office. It should also adequately plan for the change in facility usage and related costs at the district office and the campuses that result from decentralization.

- To reduce police overtime costs and overtime hours, the district should complete a police eligibility list. Campuses should hire more full-time officers and use more part-time officers to cover open shifts. These practices would reduce costs and ensure that district employees who are responsible

for promoting safety on the campuses are not overworked. Further, when the district renegotiates its contract with the police officers' union, it should consider revising provisions for assigning overtime.

- To increase its administrative flexibility, in its renegotiation of the contract with the faculty union, the district should consider increasing minimum class size, or leaving class size decisions to the discretion of district administrators; establishing a longer standard work week; and avoiding provisions that establish committees with duplicate functions.

- To provide additional benefits to the students, generate more revenues, and avoid subsidies from the general fund, the district should go forward with the one campus pilot project for fast food chains and convenience stores. If this pilot is successful, the district should encourage similar projects on other campuses.

- To assist decision makers at the state and local levels, the district should continue to communicate its unmet facilities needs by requesting funding for needed projects and maintaining up-to-date information on its long-range facilities needs. Moreover, the district should prioritize its requests for scheduled maintenance funding in conformity with those established by the Chancellor's Office of the California Community Colleges.

- To help bridge the gap between unmet facilities needs and lack of available funding, the district should explore new ways to address the improvement and maintenance of its facilities. As it achieves savings in other areas, the district should consider using these resources to meet its matching requirements for scheduled maintenance projects and to guarantee that routine maintenance is sufficient to ensure campuses are safe and attractive.

The district's long-range plan should also address its poor controls over the budgeting process. To improve the budgeting process, the district board should take the following steps:

- Establish and enforce policies and procedures that clearly define the parties the district will hold accountable for developing and adhering to budgets.

- Ensure accurate budgeting based on realistic estimates of planned activities that are justified in light of historical expenditures and detailed plans for more efficient, effective use of resources.

- Monitor college strategies for increasing revenue from various sources—including grants, contracts, and increased enrollment—and for realizing operational efficiency through improved class scheduling, staff assignment, and intercollege cooperative efforts. The board should take prompt action when the colleges or the district office project budget shortfalls.

- Ensure that controls to prevent colleges from exceeding their budgets are in place and enforced.

- Avoid using contingency reserves to cover overspending so these funds will be available for catastrophic events.

- Develop a contingency plan for the possibility that individual campuses will not be fiscally viable when subsidies from other colleges are no longer available.

As the district continues with its decentralization reforms, the board should take the following steps to ensure that decisions result in efficiencies and the careful use of resources:

- Identify what obligations the district as a whole has, both fiscally and academically, then establish who is responsible for each obligation, as well as how it will be met.

- Continue to consider carefully whether decentralization can achieve cost savings and, if so, how those savings can best be effected.

- Make college presidents' responsibilities commensurate with their authority. Follow through on the expressed intent to consult with them on issues having major impact on colleges, such as faculty salaries.

- Establish a mechanism to ensure that basic educational services at each college are not sacrificed to financial constraints.

If the district restructures the debt related to the 4050 Wilshire property by proceeding with the proposed interest rate swap/refunding transaction, it should mitigate its risk by ensuring that the indices used to set the variable rates, maturities, payment dates, and interest rate reset dates are the same for the interest rate swap agreement and the 2002 certificates of participation. In addition, it should not agree to a cancellation option in the interest rate swap agreement allowing the other party to cancel the swap if interest rates rise. Allowing such a cancellation would go against the district's objective of locking in current low interest rates.

We conducted this review under the authority vested in the California State Auditor by Section 8543 et seq. of the California Government Code and according to generally accepted governmental auditing standards. We limited our review to those areas specified in the audit scope section of this report.

Respectfully submitted,

Kurt Sjoberg

KURT R. SJOBERG
State Auditor

Date: December 23, 1998

Staff: Lois E. Benson, CPA, Audit Principal
John F. Collins II, CPA
Tone Staten, CPA
Art Martinez, CPA
Tony Nevarez
Dianna D. Scott
Wendy A. Stanek

Agency's response to the report provided as text only:

Los Angeles Community Colleges
770 Wilshire Boulevard
Los Angeles, California 90017

December 14, 1998

Mr. Kurt R. Sjoberg
State Auditor
555 Capitol Mall, Suite 300
Sacramento, CA 95814

Dear Mr. Sjoberg:

Thank you very much for the opportunity to comment on the issues you raised with respect to the bureau's draft audit of the Los Angeles Community College District. We understand that the District's comments will be included in the final audit report when issued.

GENERAL COMMENTS:

I will begin my response with an expression of concern with regard to the limited time (three working days) given to the District in which to respond to an audit that has taken some time for your staff to conduct. We believe three days to be an unreasonable time-line. 1*

As you have indicated on page 1 of the Executive Summary, your review "focused on the causes of the District's fiscal and budgetary difficulties and how the District plans to address them".

Your report identifies a number of areas where we think improvements can be made, and the District is currently addressing several of them. In February 1998, the District projected a $13.1 million ending balance deficit. Since then, the District has taken actions that enabled it to end the 1997-1998 Fiscal Year with a $2.7 million ending balance. The First Quarterly Report for 1998-99 Fiscal Year projected an ending balance of $8.3 million. This represents a $21.4 million "turn-around". This turn-around was accomplished by-

- Implementing a freeze on non-salary accounts
- Termination of many temporary employees
- Instituting a hiring freeze
- Freezing of Capital and Deferred Maintenance projects
- Expanding summer 1998 class offerings which generated additional FTES revenue

*California State Auditor's comments on this response begin on page R-5.

- Increasing State revenues for 1998-99
- Successfully resolving the District's Full-time/Part-time (75/25) dispute with the State Chancellor's Office.

The Los Angeles Community College district, similar to many other "urban" districts throughout the State in the last ten years, has experienced increased costs in excess of revenue received. It is a continuing challenge for multi-college districts, like the Los Angeles Community College District, to allocate funds and meet all the many needs of the "urban" colleges. Urban colleges have more needs than the State is willing to fund.

SPECIFIC COMMENTS:

Comments on Introduction: "The District's independent financial auditors did not raise concerns of the District's continued financial viability in the fiscal year 1997-98 Opinion, as they did for the prior year, although the District ended the year with a $3 million deficit in its Unrestricted General Fund".

(2) The District's 1997-98 audited financial statement does reflect a $3 million deficit in the unrestricted general fund ending balance. However, the District's unaudited financial statements reflect a $2.7 million positive unrestricted general fund ending balance. The difference is primarily due to the different accounting methods used to record the long term lease of the building that houses the administrative offices of the District and the faculty retirement incentive that was granted in fiscal 1994-95. The lease agreement on the building provided for two (2) years of free rent and approximately five (5) years of no operating expenses. Therefore, for the first two years of the lease there were no expenditures recorded for rent in the District's records, since the District operates on basically a "cash basis." Auditing guidelines (GAAP) does not allow for recording of lease expenses in this manner. The District's independent auditors are required to amortize the lease payments over the term of the lease to reflect the annual expense.

In 1994-95 the District granted a retirement incentive (special benefit) to the faculty. The District purchased an annuity at a cost of approximately $2.8 million annually, for five (5) years, to pay for the special benefit. The special benefit was effective July 1, 1995 and was recorded on the District's books for the first time in fiscal 1995-95 to reflect the expense in the year in which the incentive was effective. The auditors' opinion was that the expense should be reflected in the year in which the annuity was actually purchased. The cost of this first annuity was recorded in fiscal 1994-95 by the auditors which resulted in a decrease in the District's unrestricted general fund ending balance for 1994-95. This same adjustment is made each year. 1998-99 will be the last year for this adjustment.

Comments on Chapter 1: - "The District's Financial Reserves have decreased significantly."

The District is addressing its fiscal issues and expects to end the year with an adequate positive Unrestricted General Fund ending balance.

The District is projecting a $5.5 million ending balance in the Unrestricted General Fund for 1998-99. This would represent a two percent (2%) ending balance. This $5.5 million projection includes $2.901 million in prior year, 1997-98, Basic Skills revenue.

Further, the District was successful in its appeal of the 75/25 obligation penalty, and therefore, an additional $2.8 million can be added to the balance, increasing it to $8.3 million. This represents a three percent (3%) Unrestricted General Fund ending balance for 1998-99. 2

The projected ending balance of $8.3 million assumes that some of the colleges, the District Office and the Districtwide accounts will show a deficit as currently projected. However, plans are in place and/or being developed to assist the colleges and the District Office to balance their budgets and to decrease the deficit in the districtwide accounts, which, if realized, will increase the District's ending balance beyond that currently projected.

The current FTES projection is at 103.2 percent of 1997-98 and if the current trend continues, the District should realize its growth and possibly also receive a portion of the Basic Skills overcap growth funds.

Next year, 1999-2000, the District is projected to have no fiscal problems that it cannot easily address.

Comments on Chapter 1: - "The District has lacked long-range planning."

On April 29, 1998, the Board of Trustees adopted a resolution for Reform and Decentralization. The purpose of the reform is to revitalize our nine colleges to better meet the educational needs of our students. The reform calls for changes in funding to the colleges based on performance. Colleges will, over time, receive all revenue that they earn and determine which services should be decentralized and pay for those services that they want to remain centralized. The long-term implementation of reform and decentralization is currently under way. It is the Board of Trustee's commitment to make the District and its colleges operate more efficiently and to ensure accountability and greater financial and educational viability.

Comments on Chapter 1: - "The Board entered into a union agreement that significantly increased salary costs."

It is true that the District gave significant salary increases to its employees for 1996-97, 1997-98 and 1998-99. The District felt in order to recruit and retain quality faculty and staff, it was important that our employees' salaries become somewhat competitive with other surrounding comparable districts.

In an effort to reduce operating costs, the District offered an early retirement incentive program to certificated employees. The District lost 255 employees through retirement. Since that time, the District has faced a full-time/part-time teaching faculty problem, and has had particular recruitment difficulties attracting diversity among its applicants. Therefore, the District's salaries must be reasonably competitive with our neighboring

community college districts in order to attract quality faculty and staff. The District decided to make this investment.

Comments on Chapter 1: - "Excess Space for District Office Operations is costly."

It is true the District leases office space, using one building, while continuing to pay debt on another building (4050 Wilshire Boulevard) which it has never occupied and may have to sell
3 at a loss. However, it is important to understand the financial and economic climate in which the District (as well as the State) was operating subsequent to the purchase of the second building. The situation facing the District was as follows:

1. The State's economy, including the real estate market, was in a down-turn and the District (as were all other public sectors) was facing a $5 million short-fall in its 1992-93 budget.

2. The District was facing a major increase in its lease at its prior location, 617 West Seventh Street. The District was also facing a multi-year extension of that lease agreement.

3. The cost to renovate/remodel, maintain, furnish and move into the 4050 Wilshire Building was approximately $8 million.

4. The District was faced with the prospect of having to reduce college operating budgets to address the reduced apportionment and relocation costs to occupy the 4050 Wilshire Boulevard Building.

5. The process for selling the 4050 Wilshire Building was to begin immediately.

Moving into the 770 Wilshire Boulevard location was analyzed against the above situations. The District would realize short-term savings of $4.67 million from 1993-94 through 1997-98 which it would have spent had it not moved into the 770 Wilshire Boulevard building. The District would save $1.56 million in its General Fund for 1993-94. Faced with the alternatives stated in items 1 through 5 above, the decision was to move into the 770 Wilshire Boulevard building.

Further analyses were conducted by CB Commercial Real Estate Group, Inc. who arrived at
3 the same conclusions. Also, in the audit conducted by the Los Angeles County Grand Jury, it was determined that the District made the correct decision given the situation and information available at the time.

The Los Angeles Community College District appreciates the work of the State Auditor's Office in developing the report on the District. The District is continually striving to become a more responsive and effective community college district. We appreciate and accept the constructive recommendations of your team.

Sincerely,

Signed by:
James L. Heinselman

COMMENTS

California State Auditor's Comments on the Response From the Los Angeles Community College District

To provide clarity and perspective, we are commenting on the Los Angeles Community College District's (district) response to our audit report. The following numbers correspond to the numbers we have placed in the district's response.

1 In keeping with our standard practice, we allowed the district five working days to provide its response to our draft report. In addition, on multiple occasions before we provided the district with a draft, we discussed our concerns with various district office staff and board members and elicited their comments, which are included in the report. Thus, we believe the district had ample opportunity to provide its perspective. We appreciate the district's timely response to our report.

2 On page 12 of the report, we recognize that the district's unrestricted general fund ending balance for fiscal year 1997-98 differs from the balance its independent financial auditors calculated based on generally accepted accounting principles (GAAP). We have used the GAAP balance because the independent auditors have attested to its accuracy. We remain concerned that the unrestricted general fund ending balance on a GAAP basis has declined by over $12 million in the last two years to a deficit of about $3 million at the end of fiscal year 1997-98. Further, in Chapter 3, we question how effective the district's budgetary practices have been thus far in fiscal year 1998-99. As a result, we are concerned about whether the district will be successful in achieving the level of ending fund balance it currently projects.

3 On page 16 of our report, we note that the district decided not to occupy the 4050 Wilshire property because, based on a brokerage firm's analysis, it was less costly to lease different space for a district office. We also note on page 17, the grand jury's conclusion that the procedures the district followed related to its purchase of the 4050 Wilshire property and the lease for the current district office building were common practice for public

sector agencies. However, regardless of the financial and economic climate at the time these decisions were made, we reiterate our comments from pages 15 and 17 that excess space for district office operations is costly and both buildings are likely to drain district resources for years to come.

cc: Members of the Legislature
Office of the Lieutenant Governor
Attorney General
State Controller
Legislative Analyst
Assembly Office of Research
Senate Office of Research
Assembly Majority/Minority Consultants
Senate Majority/Minority Consultants
Capitol Press Corps

NOTICE

REPRODUCTION BASIS

☒ This document is covered by a signed "Reproduction Release (Blanket)" form (on file within the ERIC system), encompassing all or classes of documents from its source organization and, therefore, does not require a "Specific Document" Release form.

CA Bureau of State Audits

☐ This document is Federally-funded, or carries its own permission to reproduce, or is otherwise in the public domain and, therefore, may be reproduced by ERIC without a signed Reproduction Release form (either "Specific Document" or "Blanket").